

## Message Text

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ACTION EB-07

INFO OCT-01 EUR-12 EA-07 IO-13 ISO-00 AID-05 CIAE-00

COME-00 FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00 XMB-02

OPIC-03 SP-02 CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05

SS-15 STR-04 CEA-01 L-03 H-02 PA-01 PRS-01 AGRE-00

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P R 290635Z NOV 76  
FM AMEMBASSY CANBERRA  
TO SECSTATE WASHDC PRIORITY 9401  
INFO USDEL MTN GENEVA  
AMCONSUL MELBOURNE  
USMISSION OECD PARIS  
AMCONSUL SYDNEY  
AMEMBASSY TOKYO  
AMEMBASSY WELLINGTON  
AMCONSUL BRISBANE  
AMCONSUL PERTH

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EO 11652: NA  
TAGS: EFIN, AS  
SUBJ: NOVEMBER 29 DEVALUATION OF AUSTRALIAN DOLLAR

REF: : CANBERRA 8583 (NOTAL)

1. BEGIN SUMMARY: TREASURER'S NOVEMBER 28 ANNOUNCEMENT  
(FULL TEXT IN CANBERRA 8583) OF 17.5 PERCENT AUSTRALIAN  
DOLLAR DEVALUATION EFFECTIVE NOVEMBER 29 GREETED BY MIXED BUT  
PREDICTABLE REACTIONS FROM VARIOUS AFFECTED SECTORS. NOTE-  
WORTHY FEATURES OF NOVEMBER 28 ANNOUNCEMENT INCLUDE (1) AD-  
OPTION OF "FLEXIBLY ADMINISTERED RATE" WHICH WILL PROBABLY  
INVOLVE MORE FREQUENT AND SMALLER SHIFTS IN AUST DOLLAR  
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RELATIONSHIP TO "BASKET" OF CURRENCIES TO WHICH IT HAS BEEN

PEGGED SINCE 1974; (2) HEAVY EMPHASIS PLACED ON RECENT DECISION BY CONCILIATION AND ARBITRATION COMMISSION TO INCREASE WAGE LEVELS BY FULL AMOUNT OF SEPTEMBER QUARTER CPI INCREASE, AS IMMEDIATE REASON FOR TIMING OF DEVALUATION; (3) SIMILAR EMPHASIS ON ACCELERATING EROSION OF RESERVE POSITION THROUGH NOVEMBER 26; (4) PREVIEW OF SEVERE NEW FISCAL MONETARY AND WAGE RESTRAINT POLICIES TO CONFINE INFLATIONARY IMPACT OF DEVALUATION DECISION; AND (5) OMISSION, AT LEAST FOR THE PRESENT, OF ANY REVIVAL OF VARIABLE DEPOSIT RATE REQUIREMENT ON INCOMING FOREIGN INVESTMENT. GOA'S DECISION TO PROCEED WITH SUBSTANTIAL DEVALUATION BASICALLY MODIFIES ANTI-INFLATION TACTICS, IF NOT THE LATER STRATEGY AND PRIORITY, AND SETS STAGE FOR DIFFICULT STRUGGLE TO LIMIT IMPACT OF DEVALUATION ON 1977 WAGE LEVELS. END SUMMARY.

2. AS WAS TO BE EXPECTED, DEVALUATION WELCOMED BY MINING AND AGRICULTURAL INTERESTS. INDUSTRIAL REACTION MIXED, TAKING NOTE OF INCREASED COSTS FOR INDUSTRIAL RAW MATERIALS AND COMPONENTS. LABOR SPOKESMEN SEVERELY CRITICIZED GOVERNMENT, ESPECIALLY IN VIEW OF EMPHASIS ON WAGE RESTRAINT AND NEW AUSTERITY MEASURES IN TREASURER'S ANNOUNCEMENT, ALTHOUGH MANY IMPLIED OR CONCEDED THAT ACTION WAS UNAVOIDABLE, AND DESCRIBED NECESSITY FOR DEVALUATION AS EVIDENCE OF LIBERAL/CP GOVERNMENT'S BAD ECONOMIC MANAGEMENT.

3. AS USUAL, VIRTUALLY ALL OBSERVERS SURPRISED BY TIMING. THE REASONS FOR GOVERNMENT'S DECISION TO PROCEED AT THIS MOMENT ARE STILL A MATTER OF CONJECTURE. WHILE TREASURER'S ANNOUNCEMENT SUGGESTS RECENT FULL WAGE INDEXATION ACTION BY CONCILIATION AND ARBITRATION COMMISSION MADE IMMEDIATE ACTION NECESSARY, THIS SEEMS MORE LIKELY TO BE PLAUSIBLE REASON THAT REAL REASON FOR TIMING. THE MOST PROBABLE REASON APPEARS TO BE THE ACCELERATING EROSION OF RESERVES AS CAPITAL OUTFLOW MOUNTED IN PAST WEEKS. TREASURER'S STATEMENT CITES OCTOBER RESERVE LOSS OF AUST DOLS 269 MILLION, FOLLOWED BY FALL OF AUST DOLS 260 MILLION IN NOVEMBER 1-26 PERIOD. IN ADDITION, GOVERNMENT APPARENTLY FORESAW INCREASED LEVELS OF OUTFLOW IN DECEMBER-JANUARY PERIOD.

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4. WE UNDERSTAND MECHANICS OF DEVALUATION CONSIST OF COMPUTING NOVEMBER 29 RATES FOR FOREIGN CURRENCIES WHICH WOULD HAVE APPLIED UNDER "BASKET" APPROACH FOLLOWED SINCE 1974, THEN REDUCING EACH OF THESE RATES BY 17.5 PERCENT. THESE REDUCED RATES ARE EFFECTIVE TODAY, AND THE "BASKET" TECHNIQUE OF DAILY CALCULATION WILL CONTINUE AS IN THE PAST TWO YEARS, PROCEEDING FROM THESE NEW BASE RATES. IT IS NOTEWORTHY, HOWEVER, THAT IN FUTURE, WHILE THE "BASKET"

APPROACH WILL CONTINUE, THE GOVERNMENT PLANS TO KEEP THE RESULTING RATES UNDER CONTINUOUS REVIEW, AND EXPECTS TO BE MAKING FREQUENT FURTHER ADJUSTMENTS BETWEEN THE AUS DOL AND THE "BASKET". IN THE TREASURER'S WORDS, IT WILL BE "ADOPTING A FLEXIBLY ADMINISTERED RATE, SOMEWHAT ALONG THE LINES OF A MANAGED FLOAT". WE ASKED THE TREASURY WHETHER THESE ADJUSTMENTS IN THE RELATION TO THE "BASKET" WOULD BE PUBLICLY ANNOUNCED, OR WHETHER THEY WOULD BE INDISTINGUISHABLE FROM THE DAY-TO-DAY OPERATION OF THE "BASKET" FORMULA. TREASURY INDICATED THAT THIS HAD NOT BEEN DECIDED, BUT SUGGESTED THAT THE ADJUSTMENTS PROBABLY WOULD NOT BE PUBLICLY IDENTIFIED.

5. WITH THE EXCEPTION OF HIGHER INTEREST RATES ON TREASURY NOTES LISTED IN THE ANNOUNCEMENT, THE TREATMENT OF NEW FISCAL AND MONETARY MEASURES WHICH THE GOVERNMENT CONTEMPLATES AS A RESULT OF THE DEVALUATION IS AN OVERALL PREVIEW RATHER THAN A DEFINITIVE STATEMENT. THE ANNOUNCEMENT CLEARLY PROJECTS TIGHTENED CONTROLS ON MONEY SUPPLY, CONTINUED BUDGET AUSTERITY AND A GENERALLY HIGHER STRUCTURE OF INTEREST RATES. MANY OBSERVERS HAD PREDICTED THAT ANY SUBSTANTIAL DEVALUATION WOULD REQUIRE REESTABLISHMENT OF CONTROLS ON INCOMING FOREIGN INVESTMENT FOR MONEY SUPPLY MANAGEMENT REASONS. AT LEAST FOR THE PRESENT, HOWEVER, THE GOVERNMENT HAS APPARENTLY REJECTED THIS POSSIBILITY. PRESUMABLY THE FACT THAT STIMULATION OF FOREIGN INVESTMENT WAS ONE IMPORTANT OBJECTIVE OF THE DEVALUATION PROMPTED IT TO RELY ON OTHER MEANS OF DEALING WITH MONEY SUPPLY PROBLEMS.

6. THE IMMEDIATE EFFECT OF THE DEVALUATION ON THE INFLOW OF U.S. AND OTHER FOREIGN INVESTMENT WILL CERTAINLY BE FAVORABLE. WHILE THE POSSIBILITY OF DEVALUATION IS NOT THE ONLY FACTOR WHICH HAS DETERRED FOREIGN INVESTORS DURING LIMITED OFFICIAL USE

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THE PAST YEAR, IT HAS CERTAINLY BEEN AN IMPORTANT CONSIDERATION AND ITS IMPORTANCE HAS BEEN GROWING DURING THE RECENT MONTHS. THE LONGER RUN EFFECT WILL DEPEND UPON

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INFO OCT-01 EUR-12 EA-07 IO-13 ISO-00 AID-05 CIAE-00

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THE SUCCESS OF THE GOVERNMENT IN CURBING INFLATIONARY IMPACT AND CONTINUING ITS PROGRESS IN REDUCING AUSTRALIA'S INFLATION RATE, AS WELL AS THE CLOSELY RELATED QUESTION OF LABOR RELATIONS AND STABILITY. THE SHORT-RUN EFFECT ON U.S. EXPORTS TO AUSTRALIA (AND ON AUSTRALIAN TOURISM TO THE UNITED STATES) IS ALMOST CERTAIN TO BE ADVSERS. AMERICAN EXPORTS HAVE BEEN STRONG NOTWITHSTANDING THE LOW LEVEL OF INVESTMENT AND BUSINESS ACTIVITY, BENEFITTING IMPORTANTLY FROM THEIR FAVORABLE PRICE POSITION. IF, ON THE OTHER HAND, THE GOVERNMENT SUCCEEDS IN RESTORING AN INFLOW OF INVESTMENT AND RAISING DOMESTIC BUSINESS ACTIVITY THERE WILL BE OFFSETTING BENEFITS FOR MANY TRADITIONAL U.S. EXPORT LINES. THE MISSION PLANS DURING THE NEXT TWO WEEKS TO MAKE AN IN-

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FORMAL CANVASS OF KNOWLEDGEABLE BUSINESSMENT IN THE MAJOR TRADING CITIES TO OBTAIN THEIR INITIAL JUDGEMENTS CONCERNING THE PROBABLE EFFECT OF DEVALUATION ON U.S. EXPORTS AND WILL REPORT SEPARATELY ON THESE FINDINGS.

7. THE SUDDEN GOVERNEMTN DECISION TO DEVALUE, COMING SO

SOON AFTER THE NOVEMBER 7 PROGRAM WIDELY ADVERTISED AS AN ALTERNATIVE TO DEVALUATION, REPRESENTS A SHARP TURN-AROUND IN THE GOVERNMENT'S LONG CONTENTION THAT DEVALUATION WOULD BE INCOMPATIBLE WITH ITS ANTI-INFLATION OBJECTIVES. WHILE THE DEVALUATION MAY NOT, AS ASSERTED IN THE TREASURER'S STATEMENT REPRESENT A CHANGE IN THE BASIC ANTI-INFLATIONARY STRATEGY, IT CERTAINLY REPRESENTS A MAJOR CHANGE IN ANTI-INFLATION TACTICS. THE GOVERNMENT ALREADY FACED THE PROBABILITY OF A HIGHER RATE OF CPI INCREASE IN THE DECEMBER QUARTER THAN IN THE RECENTLY ANNOUNCED SEPTEMBER QUARTER, AND A DIFFICULT TASK IN PERSUADING THE CONCILIATION AND ARBITRATION COMMISSION TO RETURN IN THAT QUARTER TO "PARTIAL INDEXATION" IN THE INTEREST OF CONTINUING THE PROCESS OF REDUCING REAL WAGES. THE LABOR REACTION TO TODAY'S DEVALUATION SUGGESTS THAT THE INCREASE IN THE CPI WILL, IF ANYTHING, BE HIGHER THAN PREVIOUSLY EXPECTED, WHILE THE LABOR MOVEMENT'S DETERMINATION TO MAINTAIN "FULL INDEXATION" WILL BE HEIGHTENED BY ANTICIPATION OF PRICE RISES RESULTING FROM DEVALUATION. THE GOVERNMENT ACCORDINGLY NOW FACES THE USUAL POST-DEVALUATION PROBLEM OF FINDING WAYS TO PREVENT THE ADVANTAGES OF DEVALUATION FROM LEAKING AWAY DURING THE COMING YEAR IN THE FORM OF A REVERSAL OF ITS RECENT SUCCESSES AGAINST INFLATION. IT IS UNDERSTATEMENT TO SAY THAT IT FACES GREAT DIFFICULTIES.

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## Message Attributes

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